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Subsidies May Be Cut for Student Loans

Republicans' Idea Could Roil Industry

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House Republicans are considering legislation aimed at reducing government subsidies for a federally supported student loan program, a step that critics say could lead to sharp increases in the long-term cost of going to college.

The Republican proposals, which are in draft form and have not been circulated, could shake up the \$35 billion-a-year student loan industry. Among the ideas being considered, according to lobbyists for both sides, is a major revamp of the present system of permitting recent graduates to consolidate student loans at fixed interest rates.

Because it is widely believed that a rise in interest rates is inevitable, a move to variable interest rates would likely mean higher bills for millions of college graduates over the next few years. But it could permit the government to use the money saved from subsidizing artificially low interest rates to help low-income students.

As a prelude to a formal debate on the changes, today the House Committee on Education and the Workforce will hear arguments for and against fixed-rate student loans. Supporters and opponents of loan consolidation have submitted widely divergent estimates of the costs of keeping the present system for the student and the taxpayer.

A spokesman for the committee, David Schnittger, said Republican leaders are crafting a bill to reauthorize student-aid components of the Higher Education Act, which is due to expire in September. He said the Republican majority is opposed to "runaway entitlement spending" and wants to produce a bill that is "fiscally responsible."

The Republican emphasis, Schnittger said, will be on "expanding college access for low- and middle-income students who are currently aspiring to attain a higher education" rather than on providing long-term benefits to "people who aren't even students."

Under the present system, which has been in place since the mid-1980s, graduates are permitted to consolidate several student loans into a single long-term package at a favorable interest rate. Graduates have been rushing to lock in government-guaranteed 30-year interest rates of 3.5 to 4.1 percent, well below the rate offered for home mortgages.

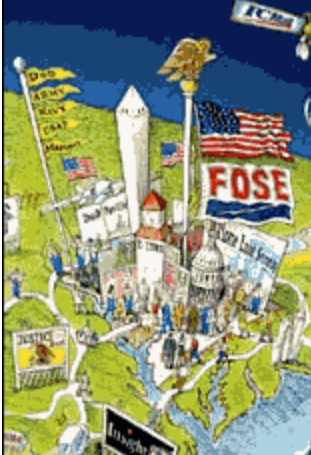
As long as interest rates are low, the program costs taxpayers nothing and may even be profitable, because the government charges lenders a service fee of about 1 percent a year for guaranteeing the loans. But if interest rates rise over the next 10 years, as many economists predict, the government would have to make up the difference between the market rate and the fixed, consolidated rate, and costs

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could soar.

The student loan industry is split on how to deal with the looming budget crunch. Most big lenders, including Sallie Mae, which claims a 29 percent share of all outstanding loans, would like to do away with consolidation on the grounds that it is becoming far too costly over the long run for taxpayers. Small loan-consolidation companies are fiercely opposed to any changes, fearing that they could be driven out of business.

Sallie Mae recently commissioned a study that predicted the consolidated loan program will cost taxpayers at least \$35 billion over the next eight years.

"The nightmare scenario is that the student loan program will hemorrhage money as interest rates go up, and Congress will be obliged to make cuts in other areas in order to pay for it," said Kevin Hassett, director of economic policy studies at the American Enterprise Institute and one of the authors of the Sallie Mae study.

Henry Howard, president of the U.S. Education Finance Group, a leading loan-consolidation company, said college graduates could end up paying twice as much in interest if the fixed-rate system is abandoned.

Most Democrats are strongly opposed to any attempt to abolish fixed-interest-rate student loans, said Rep. George Miller (Calif.), the ranking Democrat on the House education committee. But another Democrat, Rep. Robert E. Andrews (N.J.), said he would support a cutback in the program if the money saved would go to low-income students.

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